

**Olivier Guersent**  
**Director General**  
**Directorate-General for Financial**  
**Stability, Financial Services and**  
**Capital Markets Union**  
**European Commission**  
**1049 Brussels**  
**Belgium**

**Ref: Revision of the European Commission's Non-Binding Guidelines on Non-Financial Reporting**

Dear Mr Guersent,

On 20 February 2019, the European Commission (EC) published a Consultation Document seeking feedback on the update of the Non-Binding Guidelines on Non-Financial Reporting (hereinafter the 'Guidelines'). The European Securities and Markets Authority (ESMA) thanks you for the opportunity to contribute to the revision of the Guidelines. We are pleased to provide you with the following comments with the aim of improving the transparency and enforceability of non-financial statements.

The area of non-financial reporting, most notably in relation to environmental matters, is gaining momentum at European and international level, as investors and the public at large ask for more relevant and reliable information to support investment decisions in the context of sustainable finance. Particularly, at its open hearing on Sustainable Finance held on 4 February 2018<sup>1</sup>, ESMA collected the views of different stakeholders raising questions on the existing non-financial disclosure requirements and practices and their ability to support sustainable investment. ESMA, therefore, supports the EC's efforts in this area aiming at promoting high-quality non-financial disclosures.

Particularly, ESMA welcomes the EC's proposal to incorporate into the Guidelines a specific supplement focusing on climate-related information in line with the recommended disclosures of the Financial Stability Board's Task Force on Climate-Related Financial Disclosures (TCFD), as well as with disclosures arising from other relevant frameworks. We note that, in light of the lack of consistency in the disclosure practices observed in the 2017 reporting cycle, the proposal to incorporate into the Guidelines targeted requirements based on existing disclosure

---

<sup>1</sup> For more information on this open hearing, please refer to this link: <https://www.esma.europa.eu/press-news/hearings/hearing-measures-promote-sustainability-in-eu-capital-markets> .

frameworks, while not yet sufficient, goes into the right direction of helping issuers improving the comparability and quality of their non-financial disclosures.

However, we highlight that along with climate-related aspects, the other non-financial matters that are referred to in the NFRD (such as environmental, social, employee, human rights, anti-corruption and anti-bribery related aspects) are also relevant and need to be adequately disclosed. Therefore, we recommend the EC to ensure that when reviewing the Guidelines, an appropriate balance is achieved across requirements relating to the various non-financial matters, in order to avoid that the focus on one specific matter, such as climate change, detracts from the attention to the necessary disclosures on the other non-financial matters.

While generally supporting the proposals in the Consultation Document, ESMA would like to highlight the following key areas where we believe that the proposed approach to update the Guidelines could be further improved.

### *Materiality*

First of all, while ESMA welcomes the EC's clarification as to how the notion of materiality in the Non-Financial Reporting Directive (NFRD)<sup>2</sup>, as transposed into local law, should apply to climate-related disclosures, we believe that the clarifications included in the Consultation Document would also be beneficial for the main text of the Guidelines. Therefore, we encourage the EC to incorporate these clarifications into the existing section of the Guidelines relating to material information. ESMA also suggests that the proposed recommendation for issuers to disclose how they reached the conclusion that climate is not a material issue, is extended to all non-financial matters referred to in the NFRD. Furthermore, we recommend to clarify, if not directly in the text of the NFRD at least in the Guidelines, the interaction between the identification of material information and the NFRD requirement to disclose a reasoned explanation as to why a certain non-financial policy is not pursued. More generally, we highlight that the requirements of the NFRD have been incorporated as amendments to the Accounting Directive<sup>3</sup> whereas an established notion of materiality for financial reporting purposes already exists. We believe that it is important that in due course the EC considers whether and how this notion may need to be updated to take into account the specificities of materiality assessments for non-financial reporting purposes.

### *Proposed structure of disclosures*

Secondly, the Consultation Document proposes to structure the climate-related requirements into 'Type 1' and 'Type 2' disclosures, whereby the former would represent more basic or 'minimum' disclosures which issuers are expected to provide in all cases in which climate-

---

<sup>2</sup> Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.

<sup>3</sup> Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC.

related matters are material, while the latter would only be intended as providing more enhanced information. While this approach could be theoretically sound and proportionate, in practice ESMA believes that the set of disclosures currently proposed as Type 1 is still too limited and may incentivise issuers to focusing only on this category of minimum disclosures and risk promoting only a ‘tick-the-box’ approach. Furthermore, the proposed structure would be limited to the climate-related disclosures, thus creating an internal inconsistency with the other parts of the Guidelines. Therefore, we would recommend expanding the disclosures which are currently proposed as Type 1 with some of the requirements that are currently only classified as Type 2 (detailed suggestions in this regard are proposed in the Annex to this letter). In addition, we would also suggest considering the applicability of the proposed structure to the other disclosure requirements in the Guidelines.

### *Scope of the Guidelines*

Thirdly, ESMA notes that the Consultation Document makes reference to the size of the company as one of the criteria which may affect the content of the climate-related disclosures. ESMA would like to highlight that the requirements in the NFRD, which are already targeted to a selected population defined on the basis of dimensional criteria, do not envisage any additional differentiation amongst the entities that are in its scope depending on their respective size. This is particularly relevant for entities that qualify as issuers and which are subject to the requirements in the Transparency Directive. ESMA believes that, independently of their size, all issuers should ensure the same level of disclosure and investor protection and that, if a differentiation should be made in the content of the climate related disclosures, this should depend solely on the materiality of the climate-related issues.

### *Need for more robust requirements*

Finally, we take this opportunity to highlight that the evidence from the review of the 2017 non-financial statements<sup>4</sup>, while reflecting the early stage of application of the NFRD, already provides indications that support ESMA’s preliminary conclusion in its response to the EC Fitness Check on Public Corporate Reporting<sup>5</sup> that the effectiveness of the applicable requirements and the comparability of disclosures would have been greater had the NFRD indicated or established a specific disclosure framework.

While ESMA already highlighted in its 2018 statement on the European Common Enforcement Priorities the relevance of the Guidelines to improve the quality of disclosures in the non-financial statements, we note that their non-binding nature falls short of ensuring comparability and enforceability of non-financial information. In particular, questions have arisen in practice as to whether the extensive requirements in the Guidelines are consistent with the minimum required by the NFRD, thus resulting in their limited use by issuers. In order to improve the comparability and quality of the reporting, we suggest that the specificity of the requirements

---

<sup>4</sup> For a detailed description of our findings based on the review of the 2017 non-financial statements for a sample of issuers, please see ESMA’s 2018 Report on enforcement activities.

<sup>5</sup> Available at: [https://www.esma.europa.eu/file/48841/download?token=I0\\_21ZJD](https://www.esma.europa.eu/file/48841/download?token=I0_21ZJD)

in the NFRD is increased by considering in due course the incorporation in it of some or all of the requirements that are currently included in the Guidelines.

Furthermore, ESMA recommends revisiting the significant optionality (for example, the choice amongst various applicable frameworks, the location and timing of publication of the non-financial statement, the difference in enforcement powers of national competent authorities and the assurance provided) that currently characterises the NFRD to provide for a more stringent set of requirements, thus promoting consistency in disclosure and enforcement practices. This is also necessary to help filling the transparency gap that currently exists between financial and non-financial disclosures. ESMA stands ready to assist the Commission in undertaking the necessary work to that effect.

Due to the limited time available for this consultation, it was not possible to fill in the online questionnaire on the EC's website and our detailed comments to the questions raised in the targeted consultation are therefore set out in the Annex to this letter. In case you have any questions or comments, please do not hesitate to contact me or Evert van Walsum, Head of the Investors and Issuers Department ([Evert.vanWalsum@esma.europa.eu](mailto:Evert.vanWalsum@esma.europa.eu)).

Yours sincerely,

Steven Maijor

## **Annex – Responses to the questions in the online questionnaire**

### **1. Do you have any comments on Chapter 2 “How to use these guidelines”?**

1. ESMA generally supports the proposed guidance provided in Chapter 2 of the Consultation Document. However, we would like to highlight a few issues which in ESMA’s view require further consideration.
2. With respect to materiality, we note that the considerations developed in the field of climate-related disclosures can also be extended to other non-financial matters and therefore, we would recommend incorporating this guidance also into the existing text of paragraph 3.1 of the Guidelines. In this respect, we also highlight that the requirements of the NFRD have become applicable by means of amendments to the Accounting Directive whereas an established notion of materiality for financial reporting purposes already exists. We believe that it is important that in due course the EC considers whether and how this notion may need to be adapted or complemented to take into account also the specificities of non-financial reporting. For example, we note that the materiality in the non-financial information domain may require consideration of qualitative assessments to a larger extent compared to quantitative factors.
3. We support the recommendation for issuers to disclose how the conclusion that climate is not a material issue was reached, however, we believe that this recommendation should be extended to all non-financial matters referred to in the NFRD and in the Guidelines. In light of the experience from the enforcement of the non-financial statements for the 2017 reporting cycle, we would confirm that such disclosures would be particularly useful. Particularly, we have noticed that when disclosures were missing on a certain non-financial matter, only in a few cases issuers explained that the concerned non-financial matter was deemed not to be material.
4. In this respect, we note that the more general interaction between the identification of material information and the requirement in the NFRD to disclose a reasoned explanation as to why a certain non-financial policy is not pursued should also be further clarified in the Guidelines. In the enforcement experience, it is not currently possible to distinguish when disclosures on a certain policy are missing due to materiality considerations and when the issuer has failed to disclose the reason for not pursuing a policy even though the matter is regarded a material.
5. ESMA also supports the recommendation that ‘Companies are advised not to prematurely conclude that climate is not a material issue just because some climate-related risks are perceived to be long-term in nature’. However, we would recommend giving more prominence to the text in the footnote accompanying this statement which refers to publicly available materiality matrices and to expand on this by making references to specific frameworks. ESMA would also recommend complementing this statement with a reference to the fact that for their climate-related disclosures, entities are expected to leverage to the extent possible on the existing planning and forecasting capabilities used for the purpose of preparing financial accounts.

6. Similarly, we believe that the issue regarding the location of the climate-related disclosures, which in the Consultation Document is only addressed as footnote no. 16, should be discussed more in detail. Based on ESMA's experience with the 2017 non-financial statements, the use of cross-references may make the non-financial statement too fragmented thus, in some cases, impairing the understandability of the related disclosures.
7. Regarding the structure of the proposed disclosure requirements, while in principle we support the distinction between 'Type 1' and 'Type 2', we see some risks in the articulation of this distinction in the Consultation Document.
8. First of all, ESMA believes that it would be useful to clarify that, notwithstanding the articulation of the requirements into Type 1 and Type 2 disclosures, materiality should remain the driving principle when issuers assess the relevance of the information to disclose. This is particularly important to avoid that issuers overlook any Type 2 disclosures even when they could address material aspects.
9. Secondly, ESMA believes that the set of disclosures currently included as Type 1 is still quite limited and risks incentivising issuers to focusing only on the minimum information included in this category which may ultimately result only in a 'tick-the-box' exercise. Therefore, we would recommend expanding the disclosures which are currently proposed as Type 1 to include some of the specific disclosure items that are currently qualified as Type 2. In several cases, as further detailed in the responses to the other questions, our view is that some of the Type 2 disclosures, due to their importance, should be reclassified as Type 1, thus drawing into question the residual usefulness of a Type 2 category for a very few remaining items.
10. Thirdly, we note that the proposed distinction between Type 1 and Type 2 disclosure requirements does not exist in the current text of the other section of the Guidelines and therefore, making this distinction would raise a question of internal consistency within the Guidelines, once they will include the climate-related disclosure supplement. For this reason, we would recommend that the EC consider revisiting in due course also the rest of the Guidelines to achieve a consistent approach.
11. Regarding the content of the climate-related disclosures, the Consultation Document makes reference to the size of the company as one of the criteria which may affect the information reported. ESMA notes that for the entities within the scope of the NFRD, no differentiation exists on the basis of their respective size. In ESMA's view, this is particularly relevant for those entities that are required to publish a non-financial statement in accordance with the NFRD and which are also issuers that are subject to the Transparency Directive.
12. ESMA does not believe that the Guidelines should set an expectation that smaller issuers can provide disclosures of a different content compared to larger issuers. ESMA believes that all issuers, independently of their size, should ensure the same level of disclosure and investor protection and would therefore recommend that if a differentiation should be made in the content of climate-related disclosures, this should depend solely on the materiality of the climate-related issues, without any reference to the size of the issuer.

13. Finally, ESMA would like to highlight that the reference in paragraph 2.3 of the Consultation Document to the 'product life cycle approach' seems to only refer to entities involved in manufacturing activities, while a similar approach should in principle also apply to service providers, including financial institutions. Therefore, we encourage you to expand this reference to make it applicable to all entities.

## 2. Do you have any comments on Chapter 3.1 "Business Model"?

14. We support the guidance on the business model, however, we would like to suggest the following improvements.

15. First of all, the Consultation Document refers to the fact that '*To adequately report on climate related matters, companies may need to take a longer term perspective than they normally do for financial reporting*'. ESMA believes that it is important to highlight that, without prejudice to the applicable financial reporting framework, entities should consider whether the longer-term perspective that is relevant for climate-related reporting should also trigger a reconsideration of the projection and forecast horizon for financial reporting purposes. For example, this could be relevant when assessing the financial consequences of climate change in terms of risks and opportunities that may affect the present value calculations under some accounting principles.

16. ESMA would also suggest rephrasing the reference to the fact that '*Providers of capital are increasingly aware of climate-related issues and may give preference to companies with climate resilient strategies or to those that invest in low-carbon products and services*'. In ESMA's view, a more neutral wording could be used to indicate that providers of capital are interested in assessing the degree of climate resilience of strategies without necessarily referring to a preference of investors for a specific company profile.

17. In relation to the structure of the disclosure on the business model, in line with our comment in response to question 1 we would suggest expanding the list of Type 1 requirements to include the following disclosures that are currently classified as Type 2:

- a. '*how the company has selected the relevant scenarios*'; and
- b. '*the connectivity of financial and non-financial information that affect the company's strategy with regard to its portfolio of products and services, project financing activity, or asset portfolio*'.

18. Furthermore, we would like to highlight that some of the Type 2 disclosures seem to be sub-topics of the Type 1 disclosures. For example, as a Type 1 requirement issuers should describe the impact of climate-related risks and opportunities on the company's business model, strategy and financial planning, and how strategies might change to address potential transition and physical risks as well as opportunities.

19. It can be argued that, in order to fulfil this broad disclosure requirement, all the disclosures that are classified as Type 2 are necessary. For example, the disclosure of the company's dependencies on natural capital that might be at risk because of climate change or the disclosure of how any changes in the company's business model and strategy to address climate change mitigation and/or adaptation might imply changes in the company's human capital needs may be considered as part of the broader Type 1 requirement.

20. Therefore, ESMA would suggest that the EC reconsiders whether in some cases the distinction between Type 1 and Type 2 disclosures should be removed in order to avoid that Type 2 aspects that are an integral part of the Type 1 requirements are overlooked by preparers.
21. Finally, we highlight the inconsistency in the extent of the business model disclosures required in the Guidelines compared to the requirements in the NFRD. In fact, the latter refers to a *'brief explanation of the undertaking's business model'*, while the Guidelines require disclosures which are quite extensive. While we support complete disclosures on the relationship between the business model and the non-financial matters, we also note that this inconsistency may discourage issuers to use the Guidelines as a basis to comply with the minimum requirements in the NFRD. In our view, this example supports our recommendation in the response to question 9 to consider incorporating in the NFRD part or all of the requirements that are currently included in the Guidelines.

### **3. Do you have any comments on Chapter 3.2 “Policies and Due Diligence Processes”?**

22. In relation to policies and due diligence processes, ESMA considers that the following Type 2 requirements should be included as part of Type 1 as they form an integral part of what would generally be regarded as minimum information on due diligence processes:
- a. *'Explain how climate-related issues are integrated into the company's operational decision-making processes'*; and
  - b. *'Describe whether and how the company's remuneration policy takes account of climate related performance'*.

### **4. Do you have any comments on Chapter 3.3 “Outcomes”?**

23. Regarding the disclosure requirements on outcomes, ESMA believes that the following Type 2 requirement would be best referred to as a Type 1 requirement:
- *'Describe how the performance of the company with regard to climate influences its financial performance, where possible with reference to financial KPIs'*.
24. In the 2017 reporting cycle, ESMA noted that 70% of the issuers in the sample reviewed have not provided any references to, and additional explanations of, amounts reported in the annual financial statements. However, investors increasingly ask for integration between financial and non-financial information and therefore, it would be important to include the above-mentioned requirement within Type 1.

### **5. Do you have any comments on Chapter 3.4 “Principal Risks and Their Management”?**

25. Similar to what was mentioned in relation to question 2, several of the Type 2 disclosures relating to risks and risk management, seem a more detailed variation of the Type 1 requirements. We particularly believe that the following disclosures should be included as part of the Type 1 requirements as they form an integral part of a relevant description of an entity's risk management approach:

- a. *'Provide definitions of risk terminology used or references to existing risk classification frameworks used'*;
- b. *'Disclose any significant assumptions that have been used to assess climate-related risks'*;
- c. *'Describe the frequency of reviews and analyses with regard to risk identification and assessment'*;
- d. *'Describe how the company sets and applies limits to climate related risks, including any triggers used to escalate issues to management attention'*;
- e. *'Describe the processes for prioritizing climate-related risks, including any thresholds applied and indicate which risks across the value chain are considered most significant'*; and
- f. *'When relevant, disclose how scenarios and/or internal carbon pricing are used for risk management actions such as mitigation, transfer or adaptation'*.

26. Furthermore, we highlight that based on the 2017 reporting cycle, ESMA found that the connectivity between risk disclosures and disclosures of outcomes and KPIs could be improved. Therefore, we would recommend that also the following disclosure is included as Type 1:

- *'Describe the linkages between major climate-related risks and financial KPIs'*.

27. Finally, in line with previous comments on the need to integrate financial and non-financial disclosures, ESMA believes that the following disclosure should be included as Type 1:

- *'Disclose financial impacts of extreme weather events, including possible indicators on days of business interruptions and associated costs, cost of repairs, fixed-asset impairment, value chain disruptions and lost revenues'*.

## **6. Do you have any comments on Chapter 3.5 “KPIs” of the report?**

28. In relation to KPIs, ESMA notes that there are no Type 1 KPIs in relation to energy consumption and that the focus of these requirements is mainly on GHG emissions. We would therefore recommend including as part of the Type 1 KPIs the indicators relating to total energy consumption and/or production, energy efficiency targets and renewable energy and/or production targets.

## **7. Do you have any comments on Annex I “Proposed disclosures for Banks and Insurance companies”?**

29. ESMA supports the inclusion in the Guidelines of additional guidance to reflect the specificities of the financial sector as this consistent with the overall objective of aligning the Guidelines with the TCFD requirements. In this respect, ESMA welcomes the fact that the Guidelines emphasise that climate-related disclosure shall cover the potential impact on the issuers belonging to the financial sector when undertaking lending, underwriting, asset management and investment activities.

30. We note that for the disclosures relating to Banks and Insurance companies there is no reference to the distinction between Type 1 and Type 2 disclosures. While we would not be in favour of introducing such a distinction, we highlight that this is inconsistent with the proposed approach to the disclosure structure in the rest of the supplement.

**8. Do you have any comments on Annex II “Mapping of NFRD requirements and TCFD recommended disclosures” to the report?**

31. We welcome the mapping of the alignment between the TCFD and the NFRD, however we suggest the EC to double-check whether the proposed mapping covers all the relevant interactions. For example, for what concerns the disclosures on GHG emissions, these are currently marked as relating only to ‘Outcomes’ in the NFRD, while they are also relevant for the disclosures on KPIs.

**9. Do you have any additional comment?**

32. ESMA highlights that the evidence gathered from the reviews of the 2017 non-financial statements, while reflecting the early stage of application of the NFRD, already provides indications that support ESMA’s preliminary conclusions in its response to the EC Fitness Check on Public Corporate Reporting that the effectiveness of the applicable framework and the comparability of the disclosures on non-financial information would have been greater had the NFRD indicated or established a specific disclosure framework.

33. While ESMA has already highlighted in its 2018 statement on the European Common Enforcement Priorities the relevance of the Guidelines to improve the quality of non-financial disclosures, we note that due to their non-binding nature it is unlikely that the Guidelines will trigger a significant shift in the direction of more comparability and enforceability of the non-financial disclosures.

34. In particular, questions have arisen in practice as to whether the extensive requirements in the Guidelines are consistent with the minimum required by the NFRD, thus resulting in their limited use by issuers. As an example of this, please refer to our response to question 2 regarding the business model disclosures. In order to effectively improve the comparability and quality of reporting, we suggest the EC to increase the specificity of the requirements in the NFRD by considering in due course potential amendments to incorporate in the NFRD some or all of the requirements that are currently included in the Guidelines.

35. Furthermore, ESMA recommends that the areas of optionality that currently characterise the NFRD (for example, in relation to the applicable frameworks, the location and timing of publication of the non-financial statement, the difference in enforcement powers of national competent authorities and the assurance provided) be revisited to provide for a more stringent set of requirements to help filling the transparency gap that currently exists between financial and non-financial disclosures. ESMA stands ready to assist the EC in undertaking the necessary work to that effect.

36. Lastly, ESMA notes the inconsistency between the terminology used when referring collectively to environmental, climate, social, employee, anti-corruption and anti-bribery

matters as 'non-financial matters' and the fact that these aspects may have financial implications, including financial risks. Particularly, this inconsistency may give rise to some confusion especially for issuers which are not subject to the NFRD, but which are nevertheless required to prepare a management report in accordance with Articles 19 and 29 of the Accounting Directive and to include therein any principal risks and uncertainties. In this respect, we recommend the EC to further highlight that material risks may also arise from the non-financial matters and that, if this is the case, appropriate disclosures need to be provided in the management report even when an issuer is not subject to the NFRD. More in general, we encourage the EC to consider providing more clarity in the future on the possible interaction and integration between the requirements to prepare the management report and those relating to the non-financial statement.